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INFO RUCNCLS/ALL SOUTH AND CENTRAL ASIA COLLECTIVE PRIORITY
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RUEHAK/AMEMBASSY ANKARA PRIORITY 3649
RUEHBJ/AMEMBASSY BEIJING PRIORITY 1467
RUEHKO/AMEMBASSY TOKYO PRIORITY 1334
RUEHKL/AMEMBASSY KUALA LUMPUR PRIORITY 0109
RUEHAD/AMEMBASSY ABU DHABI PRIORITY 0306
RUEHIT/AMCONSUL ISTANBUL PRIORITY 1903
RUEKJCS/JOINT STAFF WASHDC PRIORITY
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SUBJECT: TECHNOCRATS AND GENERALISTS IN TURKMENISTAN'S PETROLEUM
SECTOR

11. (U) Sensitive but unclassified. Not for public Internet.

12. (SBU) SUMMARY: As Turkmenistan reforms its oil and gas industry, two principally different development strategies exist among the country's hydrocarbon leadership. One school of thought -- the technocrats -- places primary emphasis on accessing modern technology and/or services. The technocrats believe that Turkmenistan has adequate institutional, financial and human capacity to develop the country's resources (at least, onshore) independently of international oil companies. Proponents of the other approach -- the generalists -- are less categorical and interested in closer engagement and know-how transfer. While representatives of the latter approach also understand the relationship between the presence of international oil companies and the general investment climate in the country, they continue to lose the debate about future policy because they lack the technical expertise that would give them credibility. END SUMMARY

THE CONTEXT

13. (SBU) From the outset, President Gurbanguly Berdimuhamedov made a promise to bring prosperity to his people. He inherited from his predecessor, former President-for-Life Saparmurat Niyazov, an economy nearly totally dependent on the hydrocarbon industry, leaving Berdimuhamedov little choice but to continue relying on hydrocarbon revenue, at least for the foreseeable future. But with economic and rural development high on the president's list of priorities, Turkmenistan must not just sustain its current oil and gas production level, but increase it significantly.

THE TECHNOCRATS

14. (SBU) Turkmenistan's 16 years of independence have not produced a

new, modern gas and oil elite, and the old Soviet-trained hydrocarbon engineering cadre (or rather, what is left of it after Niyazov's purges of 2005) is still the dominant force in Turkmenistan's petroleum industry. This old guard - personified by Deputy Prime Minister of Gas and Oil Tachberdi Tagiyev - hold top- and mid-level management and analytical positions. These cadres, although technically competent, have had limited exposure to modern technologies and have never received formal training or significant experience in commercial and economic aspects of the oil and gas business.

15. (SBU) These technocrats, who spent their entire professional careers in a state-run system, are firmly wedded to a "we can do it all ourselves" way of thinking. In their opinion, the current industry structure can be efficient with advanced equipment. The technocrats fail to understand that Turkmenistan's reliance on foreign companies solely in a service capacity does not allow creation of a value chain - the standard across the industrialized world. They see limited value in working with international oil companies and in learning from them. However, in promoting a system of inviting international service companies and purchasing foreign hardware, they have run up against some problems:

-- The number of petroleum service companies is limited, and not all operating in Turkmenistan are of the highest technical caliber and have made some serious mistakes. For example, Turkish firm Chalik Enerji, drilling under contract for the government, had some major blowouts in 2006.

-- State oil production, which relies heavily on service operators, is declining, while the production of foreign operators, like Dragon Oil and Burren Energy, working under production sharing agreements (PSAs), is on the rise.

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-- The state's sole reliance on imported technology in an upgrade of Turkmenbashi refinery cost \$1.5 billion, but delivered low returns due to continued state control of crude and gasoline prices.

16. (SBU) Perhaps their most serious problem, however, is the gas-and-oil sector technocratic leadership's inability to engage in a full-fledged and equal partnership with gas pipeline and marketing companies. The technocrats simply do not understand the complexities of legal arrangements for joint infrastructure management and gas sales mechanisms. As a result, Turkmenistan has limited itself to a policy of selling gas at the border, ruling out alternatives that might actually increase Turkmenistan's overall profit margin.

THE GENERALISTS

17. (SBU) Most positive developments in Turkmenistan's oil and gas industry took place in the mid 1990's when a cadre of generalists emerged under the leadership of then-Deputy Chairman of the Cabinet of Ministers for Gas and Oil Yolly Gurbanmuradov. The strength of Gurbanmuradov and his team was their knowledge of the international financial system and modern business practices. During Gurbanmuradov's time in office, Turkmenistan passed a Petroleum Law laying the foundation for PSAs and establishing an agency to manage PSAs. To date, the law remains in effect. But Gurbanmuradov became too powerful and was perceived as a threat to Niyazov. The resulting purge of Gurbanmuradov and his apparatus, including the former "competent body" and Turkmenneftegaz (the body responsible for managing downstream and marketing arrangements), decimated the ranks of generalists, leaving only the unskilled behind.

18. (SBU) In March 2007, perhaps understanding the need for an agency that would be responsible for general petroleum investment issues, Berdimuhamedov re-established the former "competent body" as the State Agency for the Management and Use of Hydrocarbon Resources. President Berdimuhamedov appointed Bayrammurat Muradov, an official with banking, fiscal and financial management experience, as the Executive Director of the State Agency. As a generalist, Muradov is less categorical than his technocratic colleagues and appreciates the fact that international oil companies can bring to Turkmenistan

not only technology and capital, but also a wealth of management and marketing experience. He also understands the positive effect of an international oil company presence on the overall investment climate in the country. However, his and his team's lack of virtually any technical background in the gas and oil sector leaves them at a disadvantage in discussions with their technocratic colleagues.

¶9. (SBU) Muradov is by far a better strategist than any of the technocrats. He is of the opinion that the Government needs to set up a vertically integrated petroleum company, similar to Azerbaijan's SOCAR or Kazakhstan's KazMunaiGaz. Such a company could eliminate the coordination gap between the upstream and downstream sectors, as well as between the analytical and operational entities. More importantly, he seems to appreciate the fact that an integrated national company would be more independent and flexible -- and, ultimately, an efficient business entity. Executive Director Muradov looks further into the future and foresees a need for foreign capital. He instructed his relevant personnel to learn about the listing requirements at major stock exchanges, including the New York Stock Exchange, in preparation for the possible listing of a Turkmenistani national petroleum company.

¶10. (SBU) COMMENT: Although it seems obvious to outsiders that the two groups should be able to work together in a complementary

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fashion that is not yet possible in Turkmenistan. The country's 15 years of relative isolation from the outside world and its lack of exposure under former President Niyazov to Western management techniques have allowed issues of power, prestige and tradition to dominate business, often at the expense of profit. With the technocrats disinclined to give up any of their authority and the generalists unable, to date, to shift the focus of the debate away from solely technical issues to include a broader discussion of whether the old policies are really serving Turkmenistan's long-term interests -- an area where they should be on more even ground -- the generalists have not been able to date to sway the president into reconsidering policies of engagement with international oil companies. In the short term, continued support for a broader market-oriented approach and advocacy on behalf of U.S. oil business may ultimately convince the government to review its ways. However, in the longer term, generalists do not stand a chance without development of young petroleum professionals with mastery of market principles and advanced engineering. END COMMENT.

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